

General Information Letter: Permission is granted to request to allow nonresident partners to claim a credit for taxes paid on their behalf on a composite return.

June 19, 2001

Dear:

This is in response to your letter dated June 1, 2001, in which you request a letter ruling. The nature of your request and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 86 Ill. Adm. Code 1200.120(b) and (c), which may be found on the Department's web site at [www.revenue.state.il.us](http://www.revenue.state.il.us).

In your letter you have stated the following:

The purpose of this letter is to request, on behalf of the current partners of xxxxxxxxx xxx ("xxxxxxx"), permission to file a Composite Nonresident Return for any partnership distributions from xxxxxxxxx from September 1, 2000 through December 31, 2001, based on the facts below.

xxxxxxx is a limited liability partnership engaged in business in your state. The partnership has many individual, non-resident partners who have historically elected to be included in the xxxxxxxx Composite Nonresident Return. On June 1, 2001, xxxxxxxx will undergo a reorganization whereby the U.S. individual partners will become employees of the partnership ("reclassified individuals") and will no longer be partners of xxxxxxxx. xxxxxxxx will terminate for tax purposes (though continue as a legal entity with corporate partners), and will file short period returns for the period September 1, 2000 through May 31, 2001 because of this reorganization. Some or all of the nonresident reclassified individuals will receive distributions of taxable income allocable to your state for the period September 1, 2000 through May 31, 2001, as well as earn wages from services performed in the state for the period June 1, 2001 through December 31, 2001.

xxxxxxx respectfully requests permission to file a Composite Nonresident Return for all distributions attributable to the short period ended May 31, 2001 and requests permission to include any and all partnership distributions in this composite return.

As employees of xxxxxxxx, the reclassified individuals will be responsible for reporting their income and paying the corresponding tax on any income earned for services performed in the state from June 1, 2001 forward. As you are aware, individuals are typically prohibited from being included in a Composite Nonresident Return when they have nonresident income from other sources in the state in the same calendar year. Thus, for many of xxxxxxxxx reclassified individuals, this rule would require them to elect out of the Composite Nonresident Return for the period September 1, 2000 through May 31, 2001. The reclassified individuals would be required to make estimated tax payments on their partnership distributions and would have additional state filing requirements for the calendar year ending December 31, 2000. This requirement would create an administrative burden on xxxxxxxxx, for the nonresident

employees, and for the state. Further, it is probably that there would be no incremental benefit to the state to receive multiple nonresident individual returns and the inclusion of the partnership distribution in the nonresident individual return could potentially result in less tax to the state.

We respectfully request that you permit xxxxxxxxxx reclassified individuals to be included in the xxxxxxxxx Composite Nonresident Return that would report all partnership distributions attributable to the period September 1, 2000 through May 31, 2001. The xxxxxxxxx restructuring is a one-time, extraordinary event. We ask that in considering our request you weigh the significant burden on the reclassified employees against the state's interest in prohibiting the reclassified employees from inclusion in xxxxxxxxx Composite Return for the period September 1, 2000 through May 31, 2001.

The Department's records indicate that xxxxxxxxx has made estimated composite return tax payments on behalf of its partners for their liabilities related to its income for its taxable year beginning September 1, 2000.

### **Response**

Section 502(f) of the Illinois Income Tax Act (the "ITA"; 35 ILCS 5/101 *et seq.*) provides:

The Department may promulgate regulations to permit nonresident individual partners of the same partnership, nonresident Subchapter S corporation shareholders of the same Subchapter S corporation, and nonresident individuals transacting an insurance business in Illinois under a Lloyds plan of operation, and nonresident individual members of the same limited liability company that is treated as a partnership under Section 1501 (a)(16) of this Act, to file composite individual income tax returns reflecting the composite income of such individuals allocable to Illinois and to make composite individual income tax payments. The Department may by regulation also permit such composite returns to include the income tax owed by Illinois residents attributable to their income from partnerships, Subchapter S corporations, insurance businesses organized under a Lloyds plan of operation, or limited liability companies that are treated as partnership under Section 1501 (a)(16) of this Act, in which case such Illinois residents will be permitted to claim credits on their individual returns for their shares of the composite tax payments.

Under this authority, the Department has promulgated 86 Ill. Admin. Code Section 100.5100(e), which states:

Nonresident individuals, trusts, and estates with Illinois source income other than from a partnership, S Corporation, or Lloyd's plan of operation may, but need not, be included in a composite return. If such nonresidents are included in a composite return, they will not be permitted to claim credits on their individual returns for their shares of the composite tax payments unless the authorized agent files a petition with the Department of Revenue requesting permission for the nonresidents to claim such credit and the petition is granted. The Department shall grant the petition if the

authorized agent clearly demonstrates that no other method of filing would achieve the same degree of compliance and administrative ease for both the Department and the taxpayers. Factors to be considered will be the same as for petitions pursuant to subsection (c). The petition must be filed prior to the end of the authorized agent's taxable year, and the petition must be granted or denied prior to the due date of the return without regard to extensions. If the petition is granted, credit will be claimed by the nonresidents for their share of the composite payments in the same manner and amount as permitted resident individuals under Section 100.5160.

Your request has been timely filed under this provision. Moreover, because xxxxxxxxx has made estimated tax payments on behalf of partners for whom this request is made, it will be more burdensome for these partners and the Department these partners are not included in xxxxxxxxxx composite return and allowed a credit for taxes paid by xxxxxxxxx on their behalf. If these partners are not included in the composite return and allowed a credit, it is likely that some or all will have underpaid their estimated taxes by an amount sufficient to be subject to late payment penalty under Section 804 of the IITA. Such penalties should be abated, because the partners had reasonable cause to expect that their Illinois income tax liabilities resulting from their xxxxxxxxx income would be paid in full by xxxxxxxxx on its composite return. It would be easier for both the Department and the partners if the partners were to claim a credit for taxes paid on their behalf by xxxxxxxxx than for each partner to separately request abatement of the penalty that would result if no credit were allowed.

Accordingly, your petition is granted. xxxxxxxxx may include all of the "reclassified individuals" in its composite return for its short taxable year ending May 31, 2001, and any individual who is included on that return and also is required to include partnership income from xxxxxxxxx for that taxable year in an Illinois individual income tax return may claim a credit on his or her individual income tax return for the taxes paid on his or her behalf on the composite return. Any partner claiming such credit on a return should attach to that return a copy of this letter and a copy of the page of the attachment to the composite return showing that partner's share of the tax paid on the composite return.

As stated above, this is a general information letter which does not constitute a statement of policy that applies, interprets or prescribes the tax laws, and it is not binding on the Department. If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of the enclosed copy of Section 1200.110(b). If you have any further questions, you may contact me at (217) 782-7055.

Sincerely,

Paul S. Caselton  
Deputy General Counsel -- Income Tax